

**Verizon New England Inc.  
d/b/a Verizon Massachusetts**

**Commonwealth of Massachusetts**

**D.T.E. 01-31 Phase II**

**Respondent:** William E. Taylor  
**Title:** Senior Vice President, NERA

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-1 Please refer to the Phase II August 28, 2002, testimony of William Taylor, page 12, lines 17 to 23:

- (A) Please provide the results of all Massachusetts specific cost studies that were reviewed by Dr. Taylor in the preparation of his testimony.
- (B) Explain how the data provided in response to the prior response supports his position that economic efficiency would be improved if Verizon was provided with the flexibility to raise its local residential exchange rates.
- (C) Please provide the results of all Massachusetts specific elasticity of demand studies that were reviewed by Dr. Taylor in the preparation of his testimony.
- (D) Explain how the data provided in response to the prior response supports his position that economic efficiency would be improved if Verizon was provided with the flexibility to raise its local residential exchange rates.
- (E) Dr. Taylor states that under the plan, rates “are more likely to reflect the cost of providing services...” Please identify each service included in the word “services,” and for each of these services, identify the current rates and cost of service.

**REPLY:**

- (A) None were specifically reviewed to form conclusions in this case. Dr. Taylor’s conclusions on markups over incremental cost in Massachusetts are supported by the data provided by Verizon MA’s response to Information Request AG-VZ 3-16(A).
- (B) Reported markups of price over cost are the reverse of what an economist would expect if prices were based on Ramsey principles.

**REPLY:** AG-VZ 3-1  
(cont'd)

- (C) Please see the response to Information Request AG-VZ 1-1.
- (D) The relative orders of magnitude of the elasticity values shown in the response to Information Request AG-VZ 1-1 clearly show that efficiency would increase if basic residential service rates rose and prices of other more elastic services fell.
- (E) The statement refers to all Verizon MA services. Dr. Taylor's conclusions on markups are supported by data provided in Verizon MA's response to Information Request AG-VZ 3-16(A).

VZ # 253

**Verizon New England Inc.  
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**Commonwealth of Massachusetts  
D.T.E. 01-31 Phase II**

**Respondent:** William E. Taylor  
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**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-2 In New Mexico Public Regulation Proceeding 3325, William Taylor testified that “In a perfectly competitive market, the price of any increment of service is driven to the full economic cost of that increment of service and is, therefore, economically efficient.” Direct testimony, August 18, 2000, at 9. The testimony is identified at page 29 of 33 Exhibit WET-1.

- (A) Define the term full economic cost.
- (B) Provide the “full economic cost” of basic residential service in Massachusetts. Include in the response the supporting work papers and a narrative explanation of how this value was derived.

**REPLY:**

- (A) As the referenced testimony pointed out (pages 9-10), in real-world markets that are not “perfectly” competitive in the textbook sense (see footnote 8 in the testimony for reasons for this), pure incremental cost measures like marginal cost, LRIC, or TSLRIC do not sufficiently capture the relevant *full* economic cost. Rather, in such a market, the full economic cost must include the relevant incremental cost and, in addition, an appropriate share of other legitimate, recoverable, forward-looking shared and common costs where the appropriate share is determined by market conditions. In these circumstances, the full economic cost exceeds the incremental cost-based price floor, and the economically efficient price is set to recover that full economic cost.
- (B) Dr. Taylor performed no calculation of the full economic cost of basic residential service in Massachusetts.

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**Respondent:** William E. Taylor  
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**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-3 Please refer to William Taylor's Phase II August 28, 2002, page 14, lines 16 and 17.

- (A) Please provide any analysis, other than the cited D.T.E. decision, that supports the proposition that residential rates are below their efficient level.
- (B) Do you concur that the cost data cited by the Department in its Phase I Order at 100 (footnote 20 of Dr. Taylor's testimony) was produced in the 1980s or early 1990s? If not, explain why not?
- (C) If the answer to the prior question is affirmative, does Dr. Taylor believe that cost estimates produced in the 1980s or early 1990s provide useful information regarding the forward-looking economic cost of providing residential exchange service today? If so, explain why.

**REPLY:**

- (A) Please see the response to Information Request AG-VZ 3-1.
- (B) Dr. Taylor does not know the vintage of cost analysis referred to by the Department in its Phase I Order at 100.
- (C) Yes. Even large changes in the incremental costs of providing residential exchange service and usage services do not affect the conclusion that higher residential exchange prices and lower usage prices increase economic efficiency.

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**Respondent:** William E. Taylor  
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**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-4 Please refer to William Taylor's Phase II August 28, 2002, page 17. Lines 23 to page 17 line 13.

- (A) Does Dr. Taylor believe that customer acquisition costs (e.g., advertising) are sunk costs? If not, explain why not?
- (B) Has Dr. Taylor prepared or reviewed any data that compares the customer acquisition costs of an entrant versus an ILEC's customer acquisition costs? If so, provide the estimate(s).
- (C) Does Dr. Taylor concur that an entry barrier exists when the potential entrants face costs greater than those incurred by a firm now incumbent in the industry?
- (D) Does Dr. Taylor consider customer acquisition cost to be an entry barrier? If not, explain why not. If so, please provide an estimate of the size of the entry barrier. Include in the response the work papers associated with the cost estimate.

**REPLY:**

- (A) Customer acquisition costs (e.g., advertising costs) may be sunk in some instances but not in others. The cost of an asset is sunk if it cannot be recovered by leasing, selling, or otherwise transferring that asset. Usually, this means that the asset in question has little or no alternative use. The "asset" acquired through advertising is a customer base to which a firm intends to market its products and services. However, if that customer base has an "alternative use," i.e., it could serve an economically valuable function to another firm (such as a competitor), then the cost to acquire it may not be sunk. For example, in some telecommunications market segments like Internet service providers and cellular mobile service providers, it has been common for firms to

**REPLY:** AG-VZ 3-4  
(cont'd)

grow by acquiring other firms. In the process, the acquiring firm purchased not merely the acquired firm's physical assets but also its customers (at a prescribed cost per customer). In these circumstances, the advertising and customer-development costs of the acquired firm cannot be regarded as sunk. Furthermore, advertising costs are part of a firm's retail costs which tend often to be recovered through retail prices.

- (B) Dr. Taylor has not conducted any comparison of the customer acquisition costs of an entrant with those of an ILEC.
- (C) A long-run barrier to entry is a cost that an entrant faces but the incumbent does not and which lowers economic efficiency. Thus, an incumbent's (hypothetical) lower production costs are not generally thought to be a barrier to entry because economic efficiency is increased when output is produced by lower-cost firms.
- (D) No. Past economic research has shown that, if the incumbent has no advantage over a potential entrant in a specific customer-acquisition activity like advertising, then advertising cannot restrict entry even if the incumbent has built up a stock of goodwill from past efforts. That an entrant faces customer-acquisition costs *after* the incumbent has already faced them does not alter the fact that both incur those costs, although not at the same time. The empirical evidence on whether advertising costs can be an entry barrier in this sense is mixed and inconclusive. For example, see the discussion in Dennis W. Carlton and Jeffrey M. Perloff, *Modern Industrial Organization*, New York: Addison-Wesley, Chapter 14, especially page 466.

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**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-5 Reference Taylor Direct, Reference Page 14, lines 14 to page 15 line 13.

- (A) Please provide Dr. Taylor's forecast for the annual rate of inflation for the years 2002 through 2006 inclusive. Provide an explanation of how the forecast was constructed and the underlying data used to construct the forecast.
- (B) Provide Dr. Taylor's estimate of how the forward-looking economic cost of residential exchange service is going to move relative to inflation over the next five years. Provide the basis for the forecast. To the degree to which he has separate forecasts for the dial tone and exchange usage, include in the response forecasts for each of these rate elements.
- (C) The annual CPI rate of inflation for the years 1997 – 2002 is 2.3%. This value was derived by using data available at the BLS web site:  
<ftp://ftp.bls.gov/pub/special.requests/cpi/cpiai.txt> Ln  
(180.1/160.5) / 5. Why should a value of 5% be used, rather than the historical rate of inflation, 2.3%?

**REPLY:**

- (A) Dr. Taylor has made no such forecast.
- (B) Dr. Taylor has conducted no study to answer this question.
- (C) Dr. Taylor has conducted no study to determine the annual rate of inflation as measured by the CPI. The Department concluded that 5 percent is "roughly comparable to the historic annual change in the Consumer Price Index." Importantly, achieving efficient rate levels does not depend uniquely on underlying measures of cost and how they change over time but rather includes both supply and demand factors in the market.





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**D.T.E. 01-31 Phase II**

**Respondent:** William E. Taylor  
**Title:** Senior Vice President, NERA

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-6 Reference Direct Testimony of William Taylor, August 28, 2002, page 3, lines 1 to 15.  
What are the efficient competitive price levels of basic residential service?  
(A) Provide all work papers associated with the calculations and identify the source of the data used in the calculations.

**REPLY:** (A) Dr. Taylor has not made any calculations.

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**D.T.E. 01-31 Phase II**

**Respondent:** William E. Taylor  
**Title:** Senior Vice President, NERA

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-7 Reference Direct Testimony of William Taylor, August 28, 2002, page 4, lines 1 to 7. Explain why in light of the fundamental changes in the structure of the telecommunications markets in Massachusetts that have occurred since the passage of the 1996 Act, Dr. Taylor concludes that it is appropriate to rely on demand elasticity estimates from the pre-1996 period (see Verizon's response to AG-VZ 1-1, notes 2, 3, and 4). Include in the response an explanation of how the pre-1996 access and access + usage elasticity values reflect the "wide variety of fixed and mobile telecommunications services currently in demand."

**REPLY:** In the response to Information Request AG-VZ 1-1 Verizon MA is asked to "supply any recent estimates Verizon has of industry level and/or firm level own-price elasticities of demand." Dr. Taylor did not "conclude" that it is appropriate to rely on any particular elasticity estimates. Dr. Taylor simply provided a summary of the data readily available.

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**Respondent:** William E. Taylor  
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**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-8 Reference Direct Testimony of William Taylor, August 28, 2002, page 5, lines 18 to 20.  
(A) Are advertising and customer acquisition costs sunk costs? If not, explain why not?  
(B) If advertising costs are sunk costs, explain why Dr. Taylor believes that the level of advertising expenditures is virtually nil.

**REPLY:** (A) Please see response to Information Request AG-VZ 3-4 (A).  
(B) The portion of Dr. Taylor's testimony to which this question references concerns merely the sunk costs that a competitor would incur if it wished to self-supply the necessary wholesale network elements, such as by building its own network. Whatever the nature of advertising costs, they are small relative to the cost of building a standalone local exchange network.

**Verizon New England Inc.  
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**Respondent:** William E. Taylor  
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**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-9 Direct Testimony of William Taylor, August 28, 2002, page 8, lines 18 to 20. Using the California energy crisis of 2001 as an example of imperfect competition, explain why imperfect competition treats customers far better than imperfect regulation. Include in the response a discussion of why the price manipulations associated with Enron are an example of how imperfect competition treats customers far better than imperfect regulation.

**REPLY:** In Dr. Taylor's view, the California energy problems were problems of imperfect regulation, not imperfect competition. Retail suppliers were unable to increase retail prices when wholesale prices rose.

**Verizon New England Inc.  
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**D.T.E. 01-31 Phase II**

**Respondent:** William E. Taylor  
**Title:** Senior Vice President, NERA

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-10 Direct Testimony of William Taylor, August 28, 2002, page 9, lines 8 to 10. Explain how the current regulation of residential retail rates prevent Verizon MA from finding out exactly the characteristics of communications services for which consumers are willing to pay.

**REPLY:** Dr. Taylor's testimony explains why marketing and pricing flexibility (for a regulated incumbent like Verizon MA) is vital to ensure that competition brings the maximum possible benefit to consumers. In competitive markets with product (or service) differentiation, every firm tries to get ahead of its rivals by developing a product or service that consumers are likely to prefer to products and services already offered. The same can happen when consumers are offered choice in other dimensions, such as packages, prices, quality levels, term and volume discounts, etc. In the past, the residential retail service available from regulated incumbents like Verizon MA (or its corporate predecessors) came in the same form and price, regardless of any variations that consumers may have wished for. Today, as unregulated competitors introduce new dimensions to the plain vanilla residential retail service, consumers are making it increasingly clear that they appreciate variety, choice and packaging. In such an environment, it would be detrimental to consumer welfare to prevent Verizon MA from being able to offer the same variety and choice. Just as its unregulated rivals have the marketing and pricing flexibility to determine what consumers most want, so should Verizon MA have the ability to use that flexibility for that purpose.

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**D.T.E. 01-31 Phase II**

**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-11 Please refer to Paula Brown's Phase II August 28, 2002, page 10, lines 9 to 16.

- (A) Provide any additional information, other than the information cited at page 10, that was considered in the process of concluding that the price increase did not negatively impact residential subscriber penetration.
- (B) Explain the degree to which the analysis reported by Ms. Brown controls for the simultaneous changes in the price of other telecommunications products, income levels, and autonomous shifts in demand due to changes in taste (e.g., increased interest in Internet access)?

**REPLY:**

- (A) No other information was considered.
- (B) Ms. Brown does not report an analysis. She notes that over a period of time when residence rates were increased the residential subscriber penetration remained at about the same level.

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**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-12 For the following residential services, please provide the pricing history of the following residential products for the years 1995 through 2002 inclusive:

- (A) Call-waiting
- (B) Caller number identification
- (C) 3-way calling
- (D) voice-mail

**REPLY:** The pricing history for the regulated services is as follows:

	<u>CW</u>	<u>CID</u>	<u>3W</u>	<u>Pkg. of 3*</u>
1995	\$2.58	\$4.95	\$3.15	\$7.24
1996	\$2.58	\$4.95	\$3.15	\$7.24
1997	\$2.58	\$5.25	\$3.15	\$7.14
1998	\$2.58	\$5.40	\$3.15	\$7.14
1999	\$2.79	\$5.40	\$3.15	\$7.35
2000	\$2.84	\$5.45	\$3.55	\$7.80
2001	\$2.90	\$5.58	\$3.55	\$7.86
2002	\$2.90	\$5.58	\$3.55	\$7.86
Annual Percent Change				
	1.6%	1.8%	1.7%	1.1%

\* This is an illustration of the Custom Calling Package Discount, which includes Call Waiting, 3-Way Calling and Call Forwarding.

The Company objects to providing the pricing history on Voice Mail as it is an unregulated service. Notwithstanding this objection, the price for Voice Mail has not changed since 1995 and remains at \$5.95.

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**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-13 Reference Paula Brown's testimony of August 28, 2002, page 7, lines 9 through 18. Explain and quantify how the "revenues from the sales of ...discretionary adjunct services [have been used] to dampen the impact on residential rates." Include in the response an estimate of how much higher in 2002 the rate for basic residential telephone rates would need to be relative to today's rates if not for the pricing freedom provided for adjunct services.

**REPLY:** The question misquotes the citation contained in Ms. Brown's testimony. The testimony cites the Department's findings in D.P.U. 89-300, p. 146:

"Given the continuity and universal service considerations for residential rates, the Department finds it appropriate to continue to use the revenues from the sale of discretionary adjunct services to dampen the impact on *basic* residential telephone rates." (emphasis added)

As the Department noted in D.P.U. 89-300, the revenue from CO supplemental services substantially exceeded the revenue requirement for those services. The Department went on to note:

"Both NET and the Attorney General seem to agree that it is appropriate to use the "contribution" from the sale of these services to mitigate increases in residential rates..."  
(D.P.U.89-300, p. 146)

Verizon MA has not conducted a stand alone cost study for the residence dial tone line and residence local usage.

VZ # 265



**Verizon New England Inc.  
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**D.T.E. 01-31 Phase II**

**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-14 Reference Paul Brown's testimony of August 28, 2002, page 8, lines 3. Provide the historical average CPI data considered by Verizon. Include in the response the source for the information and the data used in the calculation of the inflation rate.

**REPLY:** Please see the attached.

VZ # 266

**Verizon New England Inc.  
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**Commonwealth of Massachusetts**

**D.T.E. 01-31 Phase II**

**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-15 Reference Paula Brown's testimony of August 28, 2002, page 8, lines 15 to page 9 line 4.

- (A) Ms. Brown states that the residence dial tone line charges have historically been below the economically efficient level. Historically, what were the economically efficient levels of the residence dial tone line charges? Provide all supporting work papers associated with the derivation of the rates.
- (B) Ms. Brown states that under Ramsey pricing principles, the residence dial tone line charge would most likely have increased in light of increasing competition. In light of the alleged increasing competition, provide Verizon's estimates of the elasticity of demand for the different products that would be included in a Ramsey pricing calculation (e.g., dial tone, exchange usage, vertical services, Intralata toll, intrastate switched access, interstate switched access, special access). For each product, identify if the estimated price elasticity is a short-run or long run value, the reason why a short-run or long run elasticity value was selected, the study from which the value was derived, and the year of the data used to estimate the elasticity of demand.
- (C) Ms. Brown states that under Ramsey pricing principles, the residence dial tone line charge would most likely have increased in light of increasing competition. In light of the alleged increasing competition, provide Verizon's estimates

**ITEM:** AG-VZ 3-15  
(cont'd)

of the marginal or incremental cost for the different products that would be included in a Ramsey pricing calculation (e.g., dial tone, exchange usage, vertical services, Intralata toll, intrastate switched access, interstate switched access, special access). For each product, identify if the estimated cost is a short- run or long run value, the reason why a short-run or long run value was selected, the study from which the value was derived, and the study period for the cost data

**REPLY:**

- (A) Ms. Brown's statement is based on historical evidence that has shown that residential rates are likely below their efficient levels, as noted by the Department in its Phase I Order. ( D.T.E. 01-31 Phase I, p. 100.) For reference please see New England Telephone and Telegraph Co., D.P.U. 89-300 (1990); New England Telephone and Telegraph Co., D.P.U. 91-30 (1991); New England Telephone and Telegraph Co., D.P.U. 92-100 (1992); and New England Telephone and Telegraph Co., D.P.U. 93-125 (1994).
- (B) The question asks for data that "would be included" in a hypothetical Ramsey pricing calculation. As such, Verizon MA is not in possession of this hypothetical data. Please see the Company's response to Information Request VZ-AG 1-1 for available information regarding the relationship of elasticity demand factors to various services.
- (C) The question asks for data that "would be included" in a hypothetical Ramsey pricing calculation. As such, Verizon MA is not in possession of this hypothetical data.

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**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-16 Reference Paula Brown's testimony of August 28, 2002, page 9, lines 23 to page 10 line 2. Ms. Brown states: "Current prices exceed marginal costs..."

- (A) Provide the analysis that shows that current prices exceed marginal cost.
- (B) Identify and provide the study associated with the cost data provided in response to part a of this question.
- (C) Whereas Ms. Brown contends that the current price of residential service exceeds the marginal cost of production, provide the calculations that support the contention that it would be efficient to further increase the price of residential services.

**REPLY:**

- A. See Attachment A to the Rebuttal Testimony of Paula L. Brown, filed September 18, 2002 in docket DTE 01-31.
- B. The unit marginal costs used in support of the material referenced in response to part A of this question were filed by the Company in dockets DPU 86-33 and DPU 93-125 as part of the respective Marginal Cost Studies. Due to the voluminous nature of the studies, a copy will be made available for inspection at the Company's offices at 125 High Street, Boston, Massachusetts, at a mutually agreeable time.
- C. See the Company's response to Information Requests AG VZ 3-15 and AG-VZ 3-1.

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**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-17 Reference Paula Brown's testimony of August 28, 2002, page 13, line 17. Provide Ms. Brown's estimate of the current efficient residence basic service price levels. Provide all work papers associated with the calculations and identify the source of the data used in the calculations.

**REPLY:** Ms. Brown's testimony is based on historical information that Residence Basic rates are likely below their efficient levels and that the proposed increases will allow them to move closer to their efficient levels.

Ms. Brown believes that determination of the economically efficient level of Residence Basic services is best left to the market itself.

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**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-18 Reference Paula Brown's testimony of August 28, 2002, page 14, lines 15 to 16.

- (A) Provide a narrative explanation of how Ms. Brown determined that the current rates are just and reasonable?
- (B) Provide all supporting data associated with Ms. Brown's determination that the current rates are just and reasonable.

**REPLY:** The Department found that the Company's rate levels were reasonable in D.T.E. 94-50, and since that time, those rates have been under various price cap restrictions that, by definition, guaranteed they change only in accordance with the Department's rules. As a result, the rates and charges have continued to be maintained at just and reasonable levels.

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**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-19 Reference Paul Brown's testimony of August 28, 2002, page 15 lines 7 to 9. Provide any and all studies that Ms. Brown has reviewed or produced that show that the current rates do not result in regulated services subsidizing competitive services.

**REPLY:** Ms. Brown's testimony on page 15 lines 7 to 9 points out that the Department raised concerns that cost-of-service regulation would facilitate the ability of a regulated company to cross-subsidize competitive services with revenues from regulated services.

Ms. Brown's review or lack of review of studies that show the current rates do not result in regulated services subsidizing competitive services has no bearing on that testimony.

Notwithstanding, Ms. Brown has not reviewed or produced such studies.

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**Respondent:** William E. Taylor  
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**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-20 Reference Paula Brown's testimony of August 28, 2002, Attachment A, Tab B, attachment III.

- (A) Provide Exhibit DTE VZ 1-10.
- (B) Are the elasticity of demand estimates contained in DTE VZ 1-10 the most recent estimates available? If not, provide the more recent studies and explain why the Company has elected to not rely on the more recent studies.
- (C) What year(s) of demand data was used to obtain the elasticity estimates contained in the exhibit?
- (D) Are the elasticity estimates long-run or short-run values? Include in the response why either a long-run or short-run value was selected and support for the assertion that the values are long run or short run values.
- (E) Would it be appropriate in a Ramsey pricing analysis to use short-run elasticity estimates but long-run elasticity estimates for the calculation of stimulation impacts? If so, explain why?
- (F) Define the terms access and toll (w/OCP)
- (G) The access  $E_p$  of  $-.24$  was calculated as follows  $-.30 * (.04856 / .03942)$ . Provide an explanation of why this calculation was made. Why does this calculation provide the  $E_p$  for access?

**REPLY:**

- (A) Please see attached
- (B) As stated in the responses to Information Request DTE-VZ 1-10, the own-price elasticity for intraLATA toll was assumed to be  $-0.30$ . Dr. Taylor does not know of any more reasonable assumption.



**REPLY: AG-VZ 3-20**  
(cont'd)

- (C) See (B) above.
- (D) The assumption was made without reference to long or short run.
- (E) It would depend on the purpose of the Ramsey pricing analysis. Short run effects are sometimes used to project the effect of a price change in a particular period, for example a test year. In general, questions of whether proposed price changes lead to higher efficiency should rely on long run elasticities.
- (F) In the response to Information Request DTE VZ 1-10 "access" refers to intraLATA access and "toll (w/OCP)" refers to intraLATA long distance service inclusive of optional calling plans.
- (G) This calculation was made to obtain the elasticity of demand for access on the assumption that changes in access charges are completely passed through as changes in toll prices.

To see why this is true let  $p_t$  and  $p_a$  be the price of toll paid by end users and the price of access paid by interexchange carriers respectively. We know by assumption that  $\partial p_t / \partial p_a \approx 1$ . By the assumption of the response to Information Request DTE VZ 1-10, the price elasticity of demand for toll service is given by:

$$\epsilon^* = \frac{\partial Q}{\partial p_t} \frac{p_t}{Q} \approx -0.30. \text{ Similarly, the price elasticity of}$$

demand for access is given by:  $\epsilon = \frac{\partial Q}{\partial p_a} \frac{p_a}{Q}$ .

Multiplying and dividing by  $p_t$ , we obtain

$$\epsilon = \frac{\partial Q}{\partial p_t} \frac{p_t}{Q} \frac{\partial p_t}{\partial p_a} \frac{p_a}{p_t}, \text{ or given the assumptions of}$$

the response to Information Request DTE VZ 1-10,

$$= -0.30 \times 1 \times (.04856/.03942)$$

$$= -0.24.$$

VZ # 272

**Verizon New England Inc.  
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**Commonwealth of Massachusetts  
D.T.E. 01-31 Phase II**

**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory  
**Respondent:** William E. Taylor  
**Title:** Senior Vice President, NERA

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-21 Reference Paula Brown's testimony of August 28, 2002, Attachment B, Massachusetts Residence Services – Rate Comparison

- (A) With respect to RCN's plan 2, is the calling area associated with this plan equivalent to the calling area of Verizon's \$16.85 flat rate calling plan? If not, which Verizon plan is most similar to RCN's plan 2?
- (B) With respect to RCN's plan 3, is the calling area associated with this plan equivalent to the calling area of Verizon's Suburban calling plan? If not, which Verizon plan is most similar to RCN's plan 3?
- (C) With respect to AT&T's Rightpack, is the calling area associated with this plan equivalent to the calling area of Verizon's \$16.85 flat rate calling plan? If not, which Verizon plan is most similar to Rightpack?
- (D) With respect to AT&T's Rightpack + Metro, is the calling area associated with this plan equivalent to the calling area of Verizon's Suburban calling plan? If not, which Verizon plan is most similar to AT&T's Rightpack + Metro?
- (E) With respect to Broadview and Plan B Communications unlimited offerings, are the calling area associated with these plans equivalent to the calling area of Verizon's \$16.85 flat rate calling plan? If not, which Verizon plan is most similar to these two CLEC offerings?
- (F) Assume that RCN's plan 2 provides the same calling area as Verizon's flat rate plan of \$16.85. Why would it be efficient for Verizon to raise the price of its flat rate plan since RCN's service would be available at a lower rate?

**ITEM:** AG-VZ 3-21

- (G) Assume that Broadview Network's and Plan B Communication's unlimited and flat rate plans provides the same calling area as Verizon's flat rate plan of \$16.85. Why would it be efficient for Verizon to raise the price of its flat rate plan since the CLEC service would be available at a lower rate.

**REPLY:**

Attachment B to Ms. Brown's testimony of August 28, 2002 contains three inadvertent errors in its statement of Verizon MA rates. A revised Attachment containing the corrections is attached.

- (A) Yes. RCN's Plan 2 covers the same calling area as Verizon's Flat Rate plan
- (B) No. RCN's Plan 3 is comparable to Verizon's Metropolitan service plan.
- (C) Yes. When RightPak was first introduced by MediaOne (now offered by AT&T), RightPak's local calling area appears to mirror that of Verizon's Flat Rate plan.
- (D) No. AT&T's RightPak + Metro calling plan is comparable to Verizon's Metropolitan plan.
- (E) Based on a review of the tariffs filed by Broadview Networks and Plan B Communications made with the Department, neither of these competitors exclude any specific calling area(s) with their unlimited service plans.
- (F) It may not always be efficient for Verizon MA to raise the price of a particular service. Indeed, Verizon MA is only asking for the flexibility to do so. Whether Verizon MA exercises its flexibility would depend on market conditions. Importantly, assuming (as the question does) that RCN's Plan 2 is exactly equivalent in all service dimensions to a service offered by Verizon MA, it would be unnecessary and inefficient to constrain (by regulation) the price Verizon MA could charge because (by assumption) the substitute services would serve to constrain market prices.
- (G) See response provided under F above.

**Verizon New England Inc.  
d/b/a Verizon Massachusetts**

**Commonwealth of Massachusetts**

**D.T.E. 01-31 Phase II**

**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-22 Provide Verizon's Engineering Handbook Customer Service ENB Manual.

**REPLY:** Verizon MA objects to this Information Request on the ground that it is not reasonably calculated to lead to the discovery of admissible evidence. Subject to and without waiving its objection, Verizon MA provides the following response.

Verizon MA believes there to be a typographical error in this question. It believes the question intended to ask for the following information:

"Provide Verizon's Engineering Handbook Customer Service **ENG** Manual."

Based on that understanding of the question, Verizon MA has published no such document. Such a manual was prepared by AT&T in approximately 1982. Although the manual is not used by Verizon MA, we have located a copy. The document is both voluminous and proprietary. The information is, accordingly, being provided only to the Department, and a copy will be made available for inspection, to the extent provided for in a mutually agreeable Protective Agreement, at the Company's offices at 125 High Street, Boston, Massachusetts, at a mutually agreeable time.

VZ # 274

**Verizon New England Inc.  
d/b/a Verizon Massachusetts**

**Commonwealth of Massachusetts**

**D.T.E. 01-31 Phase II**

**Respondent:** Paula L. Brown  
**Title:** Vice President-Regulatory

**REQUEST:** Attorney General Set #3

**DATED:** September 6, 2002

**ITEM:** AG-VZ 3-23 Provide Engineering Practice 901-350-250 (detailed distribution area planning).

**REPLY:** Verizon MA objects to this Information Request on the grounds that it is not reasonably calculated to lead to the discovery of admissible evidence. Subject to and without waiving its objection, Verizon MA provides the following response.

Verizon MA believes that this question intended to ask for BSP 901-350-250. Based on that understanding of the question, Verizon MA has published no such document. Verizon MA believes that this document was prepared by AT&T in the early 1980s.

Although the document is not used by Verizon MA, we have located a copy. The document is proprietary. The information is, being provided to the extent provided for in a mutually agreeable Protective Agreement.

VZ # 275